

Distr.
GENERAL

UNCTAD/PA/3
22 November 1993
ENGLISH ONLY

STANDING COMMITTEE ON POVERTY ALLEVIATION
Intergovernmental Group of Experts on
Poverty Alleviation
Geneva, 24 January 1994
Item 3 of the provisional agenda

MOBILIZATION OF DOMESTIC RESOURCES FOR POVERTY ALLEVIATION

Background note by the UNCTAD secretariat

GE.93 -54357

CONTENTS

Paragraphs

INTRODUCTION	1 - 5
I. DOMESTIC SAVINGS MOBILIZATION AND EXPENDITURE BY THE PUBLIC SECTOR	6 - 33
A. Public sector mobilization efforts	6 - 17
1. Fiscal measures	10 - 13
2. Reforming the tax structure in favour of the poor .	14 - 17
B. Public expenditure	18 - 33
1. Living standards under structural adjustment . . .	18 - 20
2. Intra-sectoral allocations	21 - 23
3. Expenditure and outcomes	24 - 29
4. Military expenditures	30 - 33
II. MOBILIZATION OF SAVINGS BY THE PRIVATE SECTOR	34 - 78
A. The banking system	39 - 40
B. Rural development and poverty alleviation: access to sources of funds	41 - 72
1. Commercial banks	51 - 54
2. Specialized agricultural banks	55 - 59
3. Cooperatives	60 - 62
4. The informal sector	63 - 72
C. Market-oriented approach to credit and savings for the poor	73 - 78
III. CONCLUDING REMARKS AND ISSUES FOR FURTHER DEBATE	79 - 88

ANNEX Table: Selected quasi-informal financial arrangements for the poor

INTRODUCTION

1. Poverty alleviation and reduction require actions along various axes, which can be taken only if the necessary resources are available. Resources are needed for the delivery of social services for and to the poor, including provision of the social, economic and physical infrastructure for education, health, agricultural extension services, administration, roads and other forms of transport and communications. The general population and the poor, in particular, need access to resources in order to undertake various economic activities to support themselves, or invest in productive assets so as to ensure streams of incomes for themselves or their progeny. Household expenditures on food, medicines, education, shelter, and so on, for their children is just as much "development expenditure" as government outlays. Finally, resources are needed to support macro-economic and sectoral policies conducive to growth that could benefit the poor. If countries are to achieve high and sustained rates of economic development, it is necessary to mobilize domestic financial resources to sustain the required level of investments. While experiences show that an important condition for increasing capital accumulation is the development of human resources, there is no doubt that an inadequate rate of domestic saving can hamper the rate of capital formation and thus limit the potential for growth and development and thereby the scope for poverty alleviation and reduction.

2. This note focuses on domestic financial resource mobilization for poverty alleviation and reduction. Such mobilization calls for policies concerning both the public and the private sectors.

3. Following the introduction, section I concentrates on the public sector and the effects of budgetary policies on poverty alleviation. Aspects concerned with the linkages between public enterprise reform and poverty alleviation are not dealt with here, as they will be considered in the context of the effects of structural adjustment and job creation policies which constitute another substantive agenda item inscribed on the provisional agenda for the second session of UNCTAD's Standing Committee on Poverty Alleviation. In examining budgetary policies, both the revenue and expenditure side are discussed separately, including questions relating to reallocation of resources for poverty alleviation. On the revenue side, the linkages between restructuring tax systems (structure and administration) and their impact on poverty alleviation/income distribution are discussed. For example, in most developing countries, there is still considerable scope for increasing tax revenues through widening the tax base and more efficient tax collection, especially with respect to taxes on agricultural income, wealth and fringe benefits which represent a small proportion of GNP as compared with developed countries (see table 1). This table and those which follow have been included here only to show broad orders of magnitude. Furthermore, adjustment programmes introduced under the auspices of the Bretton Woods institutions advocate a reduction in marginal rates on individual income taxes, so as to increase compliance and reduce evasion. The resulting tax structures tend to be more regressive, with revenue-neutral results. On the expenditure side, an attempt is made to address this policy area from the viewpoint of the distribution of expenditure between the poor and non-poor.

Table 1

Taxes on income, profits and capital gains as percentage of GDP

	1981	1982	1983	1984	1985	1986
World	12.46	12.26	11.51	11.43	11.82	11.69
Industrial countries	13.99	13.78	12.89	12.83	13.25	13.16
Developing countries	5.50	5.37	5.24	5.08	5.33	5.07

Source:

IMF, Government Finance Statistics Yearbook 1989, quoted in C. Somel "The State in Economic Activity : Problems of Economic Policy-making". UNCTAD Discussion Papers No.67, September 1993, Geneva.

4. Section II deals with the mobilization of resources in the private sector. A key issue in this respect is better financial intermediation. Many countries are actively pursuing programmes for increasing household savings, particularly among the rural population where most of the poor are located, and for improving the availability of private credit through better financial intermediation, restructuring of the banking sector, and better linkages between formal and informal financial sectors.

5. Concluding remarks and issues for further debate are presented in section III.

I. DOMESTIC SAVINGS MOBILIZATION AND EXPENDITURE BY THE PUBLIC SECTOR

A. Public sector mobilization efforts

6. Public-sector mobilization efforts affect both the prospect for further economic growth and the scope for general and targeted programmes for the poor. Such efforts involve both raising the rate of saving and ensuring that available resources are used efficiently and ultimately benefit the poor. Public savings, in the narrow sense, are defined as the excess of current revenues over current expenditures in annual budgets. The two factors which, in varying degrees, in most developing countries depress the contribution of the public sector to domestic savings are pressures on governments to increase current expenditures from year to year, and the political and administrative difficulties of raising tax revenues.

7. On average, government savings account for a modest 25 per cent of total savings, or about 2 to 3 per cent of GDP in most developing countries, but there is a wide range of inter-country variations. For the size of the public sector, savings can vary with the structure of the economy, the fiscal system and use of fiscal techniques, and the underlying socio-political structure in the country. Regional averages of general government expenditures and revenues as a percentage of GDP are presented in table 2.

Table 2

Average general government expenditures and revenue as percentage of GDP for 1981-1987^a

	T. Exp.	T. Rev.	Tax Rev.	Inc. Tax	G. Tax
World	30.79	35.60	29.85	11.86	7.18
Industrial countries	31.73	37.83	32.30	13.39	6.92
Developing countries	27.26	26.63	19.67	5.27	8.37
Africa	24.80	26.68	21.51	10.68	7.29
Asia	21.73	20.73	16.51	4.91	7.80
Europe	30.37	41.32	32.13	6.22	9.18
Middle East	36.81	31.76	14.58	8.34	5.23
Western Hemisphere	27.30	24.47	19.61	3.75	9.33
Oil-exporting countries	25.65	25.50	12.76	13.51	2.25
Non-oil-exporting developing countries	27.69	26.90	21.50	4.77	8.87

Source:

Calculated from IMF, Government Finance Statistics Yearbook 1989, quoted in C. Somel "The State in Economic Activity: Problems of Economic Policy-making". UNCTAD Discussion Papers No. 67, September 1993.

- a: Averages for world, developing countries, Africa, Asia, Middle East, oil-exporting countries and non-oil-exporting developing countries cover 1981-1986; averages for the Western Hemisphere cover 1981-1984.

Abbreviations:

T. Exp. : Total general government expenditure plus lending minus repayment.
T. Rev. : General government revenue.
Tax Rev. : General government tax revenue.
Inc. Tax : General government taxes on income, profits and capital gains.
G. Tax : Domestic taxes on goods and services.

8. In many developing countries where the tax base is shallow and inelastic, Governments depend on seigniorage to fill up the revenue shortfall. Such a money-creating alternative to borrowing from the banking system may have undesirable consequences on private savings' habits and propensities and the distribution of income.

9. There is an often expressed point of view that in many developing countries, Governments may be able to contribute additional savings by holding back current expenditures on production and consumption of goods that have little economic rationale, and by eliminating unnecessary subsidies and weeding out other low-productivity non-developmental expenditures. Another aspect of public sector performance believed to warrant particular scrutiny is the public enterprise which constitutes a drain on government resources if administered prices are below cost, control is bureaucratic and there is political pressure.

1. Fiscal measures

10. Fiscal policies may affect the distribution of income either in favour of or against the poor. In many cases, however, particularly in countries with low per capita income, weak administration, and social attitudes not always conducive to tax compliance, the urgent task is to improve tax performance. This proves to be difficult in many developing countries, where the tax system is unnecessarily complex and cumbersome and relatively inelastic with respect to income levels and changes in income. Simpler tax systems could in themselves help improve collection and compliance standards. Beyond this, Governments need the political will and capacity to override powerful vested interests and to arrest any erosion of the tax base through evasion and corruption.

11. Improved resource mobilization efforts of Governments are reflected in rising tax/GDP ratios. In some developing countries, particularly Asia (the Republic of Korea, Sri Lanka, Bangladesh, Nepal and Pakistan), Governments have made considerable improvements in tax collection efforts.¹

12. Many developing countries, particularly the least developed countries (LDCs), generate the bulk of domestic revenue through taxes.² International trade (import tariffs and export taxes on agricultural commodities) account for an important share of tax revenue, particularly in sub-Saharan Africa (for example, over 75 per cent in the Gambia and in Uganda). This dependence often renders the budget of these countries highly vulnerable to fluctuations in international trade and commodity prices, with consequent instability of revenue generation. Moreover, structural adjustment programmes and stabilization policies usually include the lowering of tariffs and phasing out of export taxes, often (although not always) resulting in a significant loss of revenue as usually there are no feasible immediate alternatives to taxes on international trade.

13. To counter this decline in revenues from taxes on international trade, many countries have carried out reforms of the tax structure involving both direct and indirect taxes. In developing countries, indirect taxes are predominant because they are easier to collect.³ Emphasis has been in moving away from production taxes (regarded as distortionary) to consumption taxes (considered to be less distortionary). In recent years, many countries have enhanced revenues from direct taxes on income and wealth, both personal and corporate. In the LDCs, for instance, these taxes currently contribute between 25 per cent and 30 per cent of tax revenues. In many of them, governments have begun to emphasize better collection and administration of income taxes, revenues from which rose in the second half of the 1980s.

2. Reforming the tax structure in favour of the poor

14. Central government taxes on personal income and household expenditure affect the distribution of incomes received by people. A tax system can redistribute personal income in an absolute sense by taking absolutely larger amounts from the better-off than from the poorer members of the population, provided the benefits arising from government spending of tax revenue are not distributed according to the amount paid in taxes.⁴ In effect, sometimes

taxes reduce incomes, rather than allocate them, since there is little or nothing in the way of cash transfers (negative taxes) to assist people in the lowest income groups. By income redistribution, therefore, one normally means, taking relatively more from the rich by progressive taxation, since even proportional taxes will not reduce the degree of income inequality, everybody being left, say, with 10 per cent less disposable income with a proportional income tax of 10 per cent.

15. Many of the poorer countries have direct taxation concentrating on the formal sector. In general, these taxes are regressive, accompanied by greater evasion of the more progressive tax by higher income groups. The incidence of indirect taxes is also regressive, at least as between different income groups in the main towns, for instance between the poorest households in the lower income brackets compared with those in the higher income brackets.⁵

16. From an equity point of view, progressive direct taxes are preferred over indirect taxes but from the point of view of increasing savings, it is not clear as to which type of taxes is to be preferred. If the demand for a product on which a sales tax has been levied is price-elastic, then indirect taxes are likely to reduce consumption and increase savings. However, if demand is price-inelastic then private savings could decrease, offsetting any increase in government savings. Direct taxes are paid for out of income. An increase in direct taxes on businesses is said to decrease business savings and also reduce incentives to invest and hence lower the mobilization of resources by the private sector; however, this could be offset by an increase of government investment.

17. Tax reform, particularly through reducing tax avoidance and tax evasion by closing loopholes and simplifying procedures, can raise extra resources for the social sectors. According to the United Nations Development Programme's *Human Development Report, 1991*, Ghana and Jamaica have raised their tax revenue considerably through their improved tax collection. In some cases, countries have introduced special taxes to finance social expenditure. Brazil, for instance, has created a special fund for its programmes in health, nutrition and education and for the support of small-scale farmers, financed by a 0.5 per cent surtax on sales and a 5 per cent surcharge on corporate income tax. Pakistan levied a 5 per cent surcharge on its imports to finance high priority projects in education. Extra taxes can also be levied on luxury items.

B. Public expenditure

1. Living standards under structural adjustment

18. During the late 1970s and early 1980s, large imbalances developed in the current accounts of many developing countries; these were exacerbated by the collapse in commercial bank lending and huge debt servicing burdens throughout the 1980s, with Latin America and sub-Saharan Africa particularly adversely affected. These difficulties necessitated major adjustments, with many countries turning to the IMF and the World Bank, first for stabilization programmes but later also for structural adjustment programmes. However, at least initially, design and implementation of these stabilization and structural adjustment policies, paid very little attention to the social costs of adjustment and reforms.

19. In general, adjustment involved demand-reducing measures. The resulting unemployment or decline in real wages has hurt the poor more because they lack accumulated savings, access to credit and safety nets. Moreover, the reduction in expenditure on subsidies has often undermined their consumption⁶ and those on health and education have affected their current welfare and future human capital. The overall impact of policies in individual countries has, however, varied depending on the nature and intensity of adjustment measures required, the depth and structure of poverty, inequality and vulnerability and the way adjustment policies have been designed.

20. Concern has been expressed that the poor and the vulnerable were particularly adversely affected in many countries during the first half of the 1980s, often with falling daily per capita calorie intake, rising incidence of infant mortality and malnutrition, and decline or slow-down of primary school enrolment. Overall, the economic crisis and the ensuing adjustment programmes in the 1980s are estimated to have imposed a heavy cost on the poor and other vulnerable groups such as women and children. The recognition of this heavy cost has led to the consideration of measures that could mitigate these costs as an integral part of structural adjustment programmes. (See Social Funds and Safety Nets, document UNCTAD/PA/2).⁷

2. Intra-sectoral allocations

21. Intra-sectoral allocations have a profound impact on the welfare of the poor. Table 3 shows comparative regional averages of government expenditure on main sectors as percentage of GDP. In the education sector, the issue is the competition between primary and higher schooling. In the case of health and related services, the important distinction is largely between primary health care and more expensive hospital-based curative medicine. Primary health care facilities are more beneficial to the poor than expensive hospitals which tend to benefit a few; cheaper or free universal education is preferable to highly subsidized university education that reaches a small proportion of the population.

Table 3

**Average general government expenditure item
as percentage as percentage of GDP for 1981-1987^a**

	Education	Health	SSWHCA ^b	Agriculture	Defence
World	4.91	4.77	11.99	0.93	4.11
Industrial countries	5.04	5.18	12.70	0.79	4.39
Developing countries	3.67	1.59	4.71	2.12	2.96
Africa	5.04	2.06	2.98	3.44	...
Asia	3.21	0.85	1.53	2.70	3.49
Europe	3.29	3.56	9.98	1.98	2.84
Middle East	5.06	1.84	6.87	1.46	6.31
Western Hemisphere	4.18	1.67	9.43	0.30	1.11
Oil-exporting countries	3.47	1.16	0.43	1.47	3.28
Non-oil-exporting developing countries	3.71	1.66	5.30	2.23	2.87

Source:

Calculated from IMF, Government Finance statistics Yearbook, 1989, quoted from C. Somel, op. cit.

a: Percentage of world, developing countries, Asia, Western Hemisphere, oil-exporting countries and non-oil exporting countries for education, health, social security and agriculture cover 1981-1986. Percentages of Africa for education, health and agriculture cover 1981-1982, and for social security, etc., only 1981.

b: Social security, welfare and housing, and community amenities.

22. The evidence from most developing areas, is that secondary education and hospital-based health care have been receiving considerably higher levels of

government financial support than primary education and primary health care. For example, a recent study⁸ indicated that primary education received an average of only 43.7 per cent of the recurrent expenditure allocated to education in 1983 among 32 African countries. In only 7 of these countries did the share exceed 50 per cent. As regards health, existing evidence suggests that despite the costs of curative services being far greater than community-based public health services, most countries allocate a majority of their health budgets to hospitals and non-essential drugs used by the better-off households rather than to the more basic and cost-effective health services required by the poor. For example, in Malawi, only 6.8 per cent of total health spending was allocated to preventive services in 1987-88.⁹ In Madagascar, only 27.1 per cent of the 1987 health budget was for primary health care and endemic disease control.¹⁰ Similarly, data for Ghana indicate that most of the health budget is allocated to curative services for the urban population. Even in Tanzania, often viewed as a socially progressive nation, the share of the health budget allocated to prevention is only 5.9 per cent, with 68 per cent directed towards hospital services.

23. It is in this context that one must consider to what extent reductions and stagnation in social expenditures will directly harm the poor and, more important, whether policy reform can in fact correct the inequities in the allocation of government social expenditures. The *Human Development Report, 1991*, estimated that social expenditures needed 25 to 30 per cent of the total development allocations to maintain a proper balance between economic and social progress. Many developing countries still fall short of this level. This is particularly more serious in those countries that have a legacy of neglect of the social sectors.

3. Expenditure and outcomes

24. Implicit in the concern over low levels of social sector spending is the assumption of a strong and positive relationship between government spending, especially in the social sector, and welfare outcomes, particularly in terms of health status and educational achievements. The corollary of this expected relationship is that declining government spending will be harmful to the poor, and conversely, increases will be beneficial. This implied association is rather complicated. Several caveats weaken this relation between government spending and desired outcomes.

25. Experience shows that first, as with most other subsidies, health and education subsidies are rationed, thus a large number of potential users do not have access to them. Secondly, in general, a disproportionate share of the rationed social service subsidies has been allocated to urban areas and better-off households. Consequently, private sector systems have already emerged for the rich as well as for the poor. The few budget surveys that are available clearly show that the poor are often served by charities and privately run institutions, whether they be the catholic-run health posts, as in Senegal, or the village traditional healers. Government-run programmes are either absent or often of such low quality as to discourage utilization.¹¹ Furthermore, households often find the means to pay for services that they value.

26. Another important point is that in addition to being rationed, publicly provided social services are often of poor quality, reflecting a vain attempt to stretch an inadequate budget. This low quality of service is partially due to inadequate recurrent expenditures that long predated adjustment programmes and which, even under the most optimistic growth and external financing scenarios, will not go away in many countries in the years to come.

27. Moreover, in addition to the fiscal crisis, poor management and unqualified personnel have often exacerbated the problem. For example, in the wake of the need for fiscal restraint, cuts have tended to be concentrated in non-wage items, given the political liabilities involved in laying off workers. The diminished efficacy of health workers without supplies, however, and the consequent impact on service delivery may be greater than if expenditure reductions had been across-the-board, instead of exclusively protecting civil servants.

28. In many cases, moving to a system of cost recovery will likely have advantages for the poor. This is because if the non-poor can be made to pay for the services received, even if some of the poor have to contribute, it affords the opportunity for vastly increasing revenues. This step would enable Governments to expand services and improve their quality. Furthermore, it should be emphasized that the major barriers to the poor's use of public services is usually not high monetary cost but rather unavailability and inaccessibility (in terms of remoteness, unawareness, creditworthiness, etc.). Currently, the poor pay the costs either in the form of foregone wages, owing to illness, or of payment for private-sector services in the absence of public-sector options. It is also the case that user fees would potentially provide the necessary funds to finance expenditures with large externalities, such as immunizations and AIDs control, that deserve to be subsidized and will likely benefit more than proportionately the poor. A caveat is that the poorest of the poor, if faced with user charges, will not seek help until the ailment is far advanced.

29. The above points indicate that understanding the dynamics and implications of allocative decisions requires resorting to detailed case studies, something that goes beyond the scope of this background document. Nonetheless, the composition of inputs provided by social-sector spending should be accorded greater scrutiny, and thus lead to further rationalization to ensure that maximum returns, as measured in terms of social indicators, are realized.

4. Military expenditures

30. In order to enhance economic and social progress during the 1990s, developing country governments must make maximum use of the human, financial and material resources at their disposal. Although, as a group, developing countries do not seem to allocate to defence a larger proportion of their total government expenditures than developed countries (table 4), a consensus is spreading among developing countries - on the part of the military as well as civilians - that many developing countries' military expenditures/ establishments are too large and costly to maintain and that most could be reduced in size without compromising security. Resources released thereby could be used to contribute to poverty alleviation and reduction.

Table 4

Central government expenditure on defence as percentage of GDP

	1981	1982	1983	1984	1985	1986	1987
World	3.77	4.06	4.21	4.11	4.22	4.29	4.11
Industrial countries	3.95	4.30	4.52	4.41	4.53	4.60	4.41
Developing countries	3.04	3.05	2.94	2.89	2.95	3.01	2.84
Africa	...	...	...	...	...	...	...
Asia	3.53	3.53	3.42	3.36	3.48	3.62	3.49
Europe	3.11	2.93	2.77	2.62	2.76	...	...
Middle East	6.49	6.18	5.92	6.10	6.49	6.68	...
Western Hemisphere	1.08	1.26	1.24	1.12	1.03	1.06	1.00
Oil-exporting countries	3.50	3.32	3.19	3.10	3.20	3.38	...
Non-oil-exporting developing countries	2.90	2.96	2.86	2.82	2.87	2.90	2.77

Source: IMF, Government Financial Statistics Yearbook, 1989; quoted from C. Somel, op.cit.

31. The challenge confronting developing countries is to achieve adequate levels of security at the lowest possible cost in order to increase the resources available for development purposes. Although it is up to developing country Governments to determine how much security they need and how to configure their military forces, the international community can play an important supporting role in the military reform process. In order to decrease the economic and political burden of the military sector, developing country Governments and the members of the international community might explore the opportunities for collaborative efforts in the following four areas: (a) reducing military expenditures; (b) controlling the procurement and internal trade in arms; (c) restructuring armed forces on the basis of true requirements; and (d) supporting disarmament and demobilization.

32. It is difficult to obtain an accurate accounting of military spending because of the secrecy with which many Governments surround their military budgets and the high degree of off-budget financing prevalent in developing countries. Although many developing country Governments are implementing programmes to improve transparency and accountability in the security sector, in most countries very little information about levels of expenditure, size and composition of forces, or equipment procured is made public.

33. Available information indicates that during the 1980s, nearly 5 per cent of Africa's gross national product was allocated to the security sector, making this region one of the highest spending in the world for military purposes. South Asia was second, with 3.6 per cent of GDP spent on the military; Latin America spent 1.6 per cent of GNP on it.¹² (See also table 4). This is particularly unfortunate, as the development indicators juxtaposed along-side military expenditures indicate that Africa spends more on the military than the other regions whereas Africa compares quite unfavourably with other regions in the development indicators. Data for expenditure from 1990 onwards are scanty, but fiscal constraints and the success of some conflict resolution efforts suggest that the security sector may have absorbed fewer resources in recent years.

II. MOBILIZATION OF SAVINGS BY THE PRIVATE SECTOR

34. Corporate savings tend to be limited in many developing countries, especially the low-income countries, because of the smallness of this sector, reflecting the stages of development in these economies. The bulk of savings in such countries is held by the non-corporate sector: households and unincorporated businesses. Therefore, it might be desirable that households be encouraged to hold the major part of their savings in the form of financial assets, and to replace direct, personal and informal credit transactions by indirect, formal credit arrangements.

35. In export-oriented economies, the growth of exports may have a positive influence on domestic savings, particularly corporate savings. In this regard, appropriate instruments would need to be put in place without negating the objectives of structural reforms.

36. Enhancing the contribution of the various compulsory contractual savings schemes (insurance, provident funds, etc.) can be a means to augment resources available for the social sectors. This path, however, can reduce the funds available for private savings, if returns are inadequate, which has often been the case.

37. Provision of credit to rural people and the micro-enterprise sector is one of the most important factors in inducing these people to save. This relationship needs to be examined in detail empirically in the individual countries or communities. Rural savings and finance can be shown to be influenced by income, wealth, land tenure, external resources, taxation, demography, price levels, rural market structure, technology and, last but not least, rural credit. The relative importance of these factors vary from country to country. IFAD has found that credit is more effective than other types of financing in channelling resources to the rural poor.¹³

38. The possibilities of domestic resource mobilization and the manner of raising these resources differ according to country. The newly industrializing countries and some medium-income countries which have maintained relatively high rates of income growth have generally made considerable efforts to follow policies that benefit the private sector and have allowed market mechanism to assert a relatively strong influence in allocating resources and determining prices of goods, services and factors of production.¹⁴ Most of the shortcomings in domestic resource mobilization apply largely to low-income countries characterized by heavy reliance on the agricultural sector, slow employment expansion, extreme poverty, and inefficient financial intermediation and to some middle-income, medium-growth countries that are largely primary-product exporters.

A. The banking system

39. As stated above, the main issues concern problems of access to credit by the poor: barriers to the delivery of financial services to the poor; credit, savings and the informal sector; interest rates and credit rationing. Also, there is a need to examine such issues as: ability of the poor to obtain unsubsidized credit; ability of the poor to pay for financial services; ability of the poor to save and have access to small loans.

40. Whatever the technical intricacies, it is useful to bear in mind that the banking and financial sectors, by their very nature, facilitate the mobilization of resource transfers from sectors capable of generating a "surplus". Access to these funds for productive purposes is a different issue.

B. Rural development, and poverty alleviation: access to sources of funds

41. Successful initiatives for the mobilization of resources are those that effectively target the poor. But targeting benefits to the poor requires familiarity with their needs and being able to develop a service or product that meets local demand. For example, lack of credit has been identified as one of the limiting factors in agricultural, industrial and commercial modernization of rural areas. All avenues for increasing the flow of credit to the rural poor need to be explored. The conditions of the poor in rural areas demand an injection of bank credits in adequate amounts and on favourable terms to quicken effectively the pace of growth and development.¹⁵

42. Often, existing financial markets and institutions have been perceived to be inadequate to meet the financial requirements for agricultural development and the savings capacity of small farmers regarded to be negligible by policy-makers. The principal sources of funds for agriculture in rural areas include the commercial banks, the specialized national credit and development institutions, cooperatives and the informal sector. An additional source in many countries is remittances from urban areas.

43. Improvements in the rural banking sector can effectively contribute in: encouraging banking habits among the rural population; mobilizing savings from the rural areas for the purpose of channelling some to profitable ventures; and, the development of agriculture and agro-related industries.

44. Most relevant for the poor are informal credit markets, small farm credit programmes, traditional lenders and credit programmes as well as the institutionalization of the informal sector (see table in annex). There is a need to examine these factors.

45. Analysing progress that has been achieved by policies and programmes for input supply, rural savings and credit facilities to small farmers, livestock producers and specific vulnerable groups such as women and searching for potential solutions to improve access to and use of credit by the rural poor is very important. Until the early 1980s, in most developing countries, these policies and programmes in the agricultural area had focused mainly on public intervention to fix product prices, create cooperative structures and establish monopoly commodity marketing and input supply and distribution systems. They had been based on the need to provide the major inputs - mineral fertilizers, improved seeds and agrochemicals at lowest cost so as to encourage greater use of the inputs. Extensive use was made of parastatal and cooperative enterprises for input distribution. The provision of large subsidies by the State became an important instrument for sustaining the operations of institutions which supplied the inputs at very low cost to the farmer. The experience with this approach offers clear lessons. One is that large-scale and across-the-board subsidies do not necessarily improve poor people's access to credit or savings. Another is that subsidised credit, without incentives and infrastructure is likely to remain a permanent debt burden as borrowers have limited options for productive investments.

46. At the same time, certain Governments have pursued a top-down approach to rural finance, the objective being to improve the availability of agricultural credit services to small farmers, livestock producers and other specific, vulnerable groups, including women. The main policy instrument employed to attain this goal has been the creation of government-owned agricultural credit banks (agricultural cooperatives and development banks) financed mainly from external aid programmes (but also from budgetary/Central Bank resources), targeted to specific farmer groups, and applying fixed, subsidized interest rates. Another instrument has been the integration of agricultural credit into rural development projects.

47. The operations of these government-owned credit institutions or of the commercial banks have not always contributed to the building of viable financial institutions for the poor. Low product prices, lack of appropriate technological packages, lack of marketing including input services and infrastructure and

Governments' insistence that the interest charged by the banks be kept low, have all been major constraints to developing effective agricultural credit programmes. Under these circumstances, formal financial institutions have not reached mainly poor people. It is estimated that, in Africa, formal institutions have not reached more than 10 per cent of poor farmers, the majority of whom must still depend upon the informal financial market in some regions.¹⁶

48. Similarly, bureaucratic procedures, inefficient management, long delays in processing loan applications and high marketing margins have often made the monopoly parastatals and cooperatives ineffective mechanisms for input distribution or the promotion of new technologies for small farmers, livestock producers, and also women.

49. Many countries are handicapped by a dearth of information based on concrete analysis of case studies to guide policy decisions on the relative roles to be given to public and private sectors in input supply and credit to small farmers. Timely access to supplies by distributors, incentive prices that cover essential costs, availability of credit for financing input supply and distribution, suitable marketing and transportation infrastructure and timely ordering and scheduling of input supplies and deliveries are also critical requirements for an efficient input distribution system.

50. This experience, along with pressure from international financing agencies has, in recent years, sparked the need for change in policies and programmes for input supply and rural finance. The period since 1985 or later has, therefore, seen many countries experimenting with new ideas in this regard. Many countries are now pursuing a bottom-up approach to rural finance and credit to small farmers, livestock raisers and women which focuses on savings mobilization, a demand-led finance policy and viability of the institutions.

1. Commercial banks

51. Commercial bank lending in developing countries has tended to cluster in urban conglomerations, concentrating on funding large farming enterprises, consumer-based industries and the foreign trade sector. For instance, in 1979, only 494 bank branches operated throughout Nigeria; and more than 100 were located in Lagos.¹⁷ In Madagascar, 85 per cent of the total volume of credit granted by the four existing banks in 1975 was earmarked for foreign-owned undertakings well integrated into the external economy. Credit to trade was larger than credit extended for the production and processing of agricultural products - the former being 37.1 per cent and the latter merely 29.1 per cent of total credit volume.¹⁸ In Ghana, the commercial banks which mobilize nearly all the available savings in the country devote less than 13 per cent of their total loans to agriculture, and nearly all of this is taken up by relatively large commercial farmers.¹⁹ In general, very little credit gets to the peasant in the rural areas. The commercial banking systems in Tanzania and Zambia deploy a large share of their credit portfolio for financing large-scale agricultural undertakings. In many countries, direct participation in agricultural credit by the commercial banking system is limited. During the 1970s and 1980s, in Ethiopia, for example, the Commercial Bank of Ethiopia's lending to agriculture stagnated as the burden of meeting the seasonal and investment credit needs of State farms and peasant cooperatives was shifted to the Agricultural and Industrial Development Bank. In Kenya, commercial banks actually direct funds (30 per cent of gross domestic product)²⁰ from rural to urban areas, depriving agriculture of one of the major ingredients for sustained economic growth. The opportunity to lend to large creditworthy clients in the towns leaves them no incentive to tackle the much harder job of getting credit to small-scale farms.²¹ Unfortunately, particularly for the bulk of the developing African countries, the potential for using their network of bank branches to finance small-holder agriculture has not been effectively harnessed.

52. This is in contrast to the experience on the Indian sub-continent, where the State Bank of India (the largest commercial bank) was the pioneer in financing small-holder agriculture to an appreciable degree. Besides opening branches in rural areas on a large scale, commercial banks have set up

specialized branches. The aim of the specialized branches (Agricultural Development Branches) is to finance agricultural development and not merely agriculture. The focus of an Agricultural Development Branch, which in the initial years dealt with agricultural credit, was modified in May 1976 to include cottage and small agro-based industries, artisans engaged in rural arts and crafts and small units devoted to repairs and rural trade.

53. Apart from these specialized branches, almost all commercial banks have launched a village adoption scheme. The scheme, with its emphasis on an area-by-area approach, was first conceived by the State Bank of India in 1969 and represented a reaction to scattered lending. The initial effort to intensify agricultural lending on an area basis later gave way to the "adopted village" concept, encompassing schemes of development that covered the entire gamut of economic activities in a village. The attractiveness of the scheme to a bank lay in the easy assessment of financial needs, lower costs of operation, better supervision, better deployment of staff and transport, easier and better recovery, avoidance of duplication of financing, better coordination between bank and development agencies, and a build-up of rapport between bank and client.²²

54. Overall, it is clear that formal financial institutions are suited to meet the demand for large and long-term credit because of their reliance upon the pooling of funds from deposits and maturity transformation. Moreover, in their operations they can also exploit economies of scale and of scope. Their structure is conducive to meeting the financial needs of larger industrial and commercial units, as well as those of affluent households, but they are not suitable for providing financial services to small farmers, small-scale entrepreneurs and the poor.

2. Specialized agricultural banks

55. Specialized agricultural banks have distinctive functions and requirements which include the supervision of the productive activities of their clientele, a rigorous project-appraisal exercise, different performance criteria and different skill requirements for their staff. They rely heavily on foreign loans and government contributions. They are financial intermediaries in the very restricted sense that they extend credit but rarely mobilize savings. They face a number of problems, starting with non-performing loans. Moreover, their fixed interest rates barely cover their average operating costs; these rates are rarely revised to allow for prevailing levels of inflation. As a result, the purchasing power of their portfolios tends to diminish. Their operating costs, including non-repayment or default, may run high as a proportion of total outstanding loans per annum. The high operating cost and the woefully slow loan recovery cycle erodes their capital base for onward lending to a diversified set of customers.²³

56. In some cases, debt service and amortization consume large portions of any new resources allocated. This reduces the sums available for new lending to farmers. The banks are obliged to service their foreign debts in the currencies in which the debts are denominated. Since depreciation of the local currency will immediately raise the local currency value of debts denominated in foreign currency, foreign exchange risks are associated with the foreign currency debts of rural banks.

57. Thus it appears that, like the commercial banking system, the specialized agricultural banks have not, in general, had an appreciable impact on smallholder agriculture.²⁴ Loans are usually channelled to big commercial farmers while the small unmechanized, rain-fed agricultural operations tend to be neglected. The operational effectiveness of these development banks is often undermined by their failure to consider the views and interests of their intended clientele. More often than not, the board of directors of agricultural banks do not comprise any representatives of the farming community which the banks are designed to serve. In the majority of cases, the members of banks' boards of directors are primarily well-established businessmen, industrialists and officials from development ministries which may have subscribed to the banks' share capital. Hence their

main preoccupation may not necessarily be a concern for the distributional effects of their policies.

58. Statistical comparison of the performance of development banks is hindered by the paucity of the data base. Very few countries provide information on loans classified by the type of farmer, size of the loan, duration, size of farms and type of project. Development banks tend to be wary of risk, and few are operationally aggressive. They are basically retailers of state loan funds or channels for official development grants but rarely mobilize domestic resources.²⁵

59. Attempts to improve the lot of the agricultural small-holders have been made in some countries. The Ghana Agricultural Development Bank, for instance, has put in place the "Group Lending Programme" to suit the credit needs of small-scale farmers. Currently, the Bank has as many as 19 credit schemes, of which six are for food crops while the remaining 13 are for industrial crops. In the early 1980s, a total of 354,000 farmers or 15.7 per cent of Ghana's small-scale farming population had been reached.²⁶ The "Caisse Nationale de credit agricole" in Morocco became a relatively efficient lender to small farmers largely through the application of a number of organizational innovations. Credit to small farmers has primarily been issued for cereal production and livestock fattening. In 1977, some 67 per cent of the 323,830 borrowers from the Caisse, holding 24 per cent of its loan amounts outstanding, were identified as small farmers.²⁷ In Malawi, the Group Credit Scheme has supported improved crop production, increased small farmers' coverage at reduced costs and achieved excellent repayment performance.

3. Cooperatives

60. With rare exceptions, the cooperative movement, which was intended to spearhead a process of rural transformation, has been unsuccessful. It has not been associated with desired increases in rural incomes. In Tanzania, where there is a strong government commitment to the cooperative system of production, past years had witnessed continuing declines in output and hence incomes.²⁸ In Ghana, where successive governments since 1966 had concentrated their efforts on creating an effective cooperative system, the income of the rural people worsened by 15 per cent between 1970 and 1983. Available data on Ghana also indicated that the productivity of cooperatives is less than that of individually owned farms.²⁹ An ILO study on cooperatives also concluded that they were seldom successful in motivating and mobilizing their membership.³⁰

61. In many cases, the motivation for joining cooperatives is not purely to engage in more productive work. A study prepared for ECA showed that, in Guinea, members of cooperatives were "less motivated by collective work than a preoccupation to get benefits".³¹ In Mozambique, where there is an acute shortage of producers' and consumers' goods and where such supplies are controlled by government, the main reason for joining cooperatives is "to legitimize one's demands for such goods". In Tanzania, a major reason for joining is "to get government-promised goods". It can, therefore, be concluded that desire for generous government resources can be a motivation for joining cooperatives.

62. Some of the problems that seem to be widely prevalent in cooperatives and which make them inefficient, in general, and for the poor, in particular, are: (a) a hasty launching of cooperatives, usually before the members understand them; (b) an inexperienced management; (c) units that cannot support themselves financially; (d) a lack of supporting infrastructure, including training and financial facilities, extension services, legislation, etc.; (e) top-down politico-bureaucratic channels, and (f) lack of incentives.

4. The informal sector

63. The above shows that, in general, the structure of formal institutions is inadequate to provide financial services for small farmers, small-scale entrepreneurs and the poor. A promising approach to resource mobilization by

the private sector is based on a different premise. Instead of focusing on traditional financial intermediation, it would focus on removing other barriers to resource mobilization by and for the poor. These barriers include, for example, insurmountable collateral requirements, adverse selection, and low levels of literacy and numeracy among the poor that constrain their access to formal sectors. Saving institutions are both informal and quasi-formal.

64. Informal finance includes: family and friends who provide most of the savings facilities and loans to the poor; money-lenders; pawn-brokers; and saving and loan associations. Informal financial agents, for example, know their clients better than formal banks do which reduces information costs; but despite their popularity and potential, most of informal finance has limitations. They are segmented from larger markets which reduces competition and limits their ability to mobilize resources.

65. Quasi-formal alternatives may give greater scope for expansion. Over the past 10 to 15 years, a number of quasi-formal programmes, such as the Grameen Bank in Bangladesh and the Badan Kredit Kecamatan in Indonesia have provided poor people with access to financial services and therefore facilitated resource mobilization. A list of such 16 savings and credit institutions in ten countries is annexed. Certain characteristics of the quasi-formal finance seem to appeal to poor people:

- (a) Low transaction costs;
- (b) Immediacy of deposit and disbursement;
- (c) The lender's willingness to extend small loans; and
- (d) Flexible repayment schedules because the financier is familiar with the borrower's situation.

66. Unfortunately, Governments tend to be wary of the informal sector, as it is perceived to undermine both financial sector policies and monetary policies. In general, interest rates and credit availability in the informal sector tend to respond to aggregate monetary policy in the intended direction, as strong linkages existed between the two sectors.

67. The main advantage of the informal sector over the formal sector lies, as indicated above, in its lower transaction costs, which results from the specialization in small loans to clients. The lower costs can also be attributed to an absence of legal service requirements and to the minimal regulation compared to lenders in the formal sector. Informal entrepreneurs' comparative advantages reside in, for example, not paying pay-roll taxes or observing minimum-wage regulations, disregard of building standards, sanitary regulations, property taxes, etc.

68. As a consequence of the nature of its operations and its cost advantage, the informal sector is better suited to service the segments of the economy that are neglected by the formal sector. Thus, for instance, many small-scale farmers and entrepreneurs lack the collateral usually required by formal lenders; informal lenders usually do not require it as they are able to base their credit extension decision on personal information about the borrower or on community ties. Borrowers in general need very small amounts of credit or loans of very short duration, which informal lenders could provide profitably because of their low transaction costs; informal lenders can better meet credit demands on short notice. The informal sector can also bypass government credit controls intended to channel credit to certain priority sectors. For example, informal lenders may provide to the poor consumption loans or real-estate loans in countries where credit for those purposes is strictly controlled.

69. Group finance, in various forms, has evolved in many developing countries into an important form of informal credit through the pooling of savings deposits to generate funds for lending to members, and sometimes to non-members as well. It provides access to credit for group members and also the incentive and means to save in financial assets. The funds are sometimes deposited in formal financial institutions. These groups are found in both rural and urban areas

of lower income developing countries. Some fall into the category of rotating savings and credit associations (ROSCAs).

70. ROSCAs are found on every continent. They are known by various names: contribution club, slate, mutual lending society, pooling club, thrift groups, friendly society, rotating credit association, temporary loan association and tontine.¹² The expansion in the practice as well as in the types of ROSCAs definitely points towards a service lack, and therefore a demand for two forms of economic systems: (a) a simple and convenient outlet for savings; and (b) a convenient meeting point between deficit and surplus units, which provides attractive yields to surplus units. The speed and convenience to the surplus and deficit units, added to the fact that the financial institutions seldom considered middle-class householders, the small businessmen and the poor to be eligible for credit facilities, has resulted in the innovative outgrowth of the ROSCAs system.¹³

71. The ROSCAs, therefore, serve as an alternative device for the mobilization of savings to generate funds to serve the poor. As indicated by a number of surveys, the informal credit market - of which ROSCAs as a major component - forms an important sector of the economy. The size of the informal credit market in urban India has been estimated to be at least 20 per cent of commercial credit.¹⁴ A Central Bank of Malaysia survey reported that 75 per cent of the rural credit in the country was accounted for by the informal credit market.¹⁵ These, and many similar findings, strongly suggest that ROSCAs definitely assist in capital formation and consequently contribute towards the economic growth of the country - particularly in the sectors closely concerned with the poor, such as small-scale agriculture and business and micro-enterprises.

72. It has been demonstrated, particularly by IFAD, that group liability can effectively replace land-based or other forms of collateral in lending operations. This is of importance to the poor, who have few assets, or none at all, to offer as collateral. Although they take on many different forms in the various environments in which poor people live, these grassroots groups all operate on similar principles. Their strength lies in their social cohesiveness, rooted in their traditions and socioeconomic reality. Managing money instils a sense of responsibility, which leads to a greater sense of solidarity. The pressure inside the group guarantees that individual borrowers respect the terms of their loan agreement, especially as this is a prerequisite for the receipt of further loans. In fact, the rates of repayment in several well-designed, properly implemented projects around the world are generally higher than 90 per cent.¹⁶

C. Market-oriented approach to credit and savings for the poor

73. Credit programmes for the poor have generally been set up on the assumption that the poor cannot pay the real cost of credit and that the poor cannot save. Accordingly, credit schemes have involved subsidized rates of interest and there has been a tendency to create solely credit programmes instead of offering a viable arrangement that would enable the poor to accumulate savings as well. These schemes have also been characterized by an orientation towards social welfare in terms of staff skills and attitude. In other words, the poor have been seen as "beneficiaries" rather than "clients". While there are understandable reasons for this approach, experience shows that it has not been particularly effective, as recovery rates have been generally low and mobilization of savings has been low. This approach has resulted in retarding the development of a commercial or a cost-effective method of credit delivery and has resulted in a rapid depletion of the value of loan funds. Studies indicate that a more commercial approach to the provision of credit and mobilization of savings would tend to provide financial services that meet needs of the poor, have good recovery, mobilize savings and become sustainable.¹⁷

74. First there is the issue of interest rates. Realistic interest rates ensure the viability of the credit schemes, enabling lending institutions to meet their administrative costs and build up a base which will make their lending

operations to the poor sustainable on a long-term basis. At the same time, realistic interest rates promote savings, thereby again reinforcing sustainable lending activities.

75. Secondly, there is the issue of credit control or rationing. As pointed out earlier, Governments in many developing countries have tended to make control over finance an important tool of their development strategies, resulting in financial institutions being required to lend not so much on the basis of normal banking considerations but on government edicts. This has tended to lead to the contraction of the institutional financial sector, depleting its ability to provide financial services.

76. The low level of savings and credit services by the majority of the economically active population in developing countries severely hampers their ability to mobilize domestic resources. The problems are greater for the poorer segments of the population. To reach informal sector borrowers and savers requires the ability to provide lending and services capable of making numerous small loans on a largely unsecured basis and capturing savings of similar amounts.

77. Examples of successful projects such as the Grameen Bank (Bangladesh), the Bank Rakyat (Indonesia) and Predom (Bolivia) all illustrate that the quasi-formal commercial approach can be effective. These three programmes, while operating in radically different contexts, focus on low income populations and enable the following generalizations to be made:

- (a) **The poor can afford unsubsidized credit.** Cases such as the three cited above point to the fact that although, like the case of Grameen, a subsidy exists borrowers could still pay a rate that would make the bank profitable. The recovery rate of loans is recorded at 99 per cent, something which regular banks in Bangladesh, where the average rate of default is particularly high, have never approached. This performance indicates an awareness on the part of the borrowers of the importance credit has in lifting them out of destitution. The Grameen Bank, in particular, now stands as a model of lending to the poor, with a very real possibility of being reproduced, not only in the poorest countries, but also in the heart of the richest ones, as witnessed by a project for a similar scheme targeted at low-income women in Chicago (United States of America);
- (b) **The poor can be creditworthy.** Evidence indicates that the economic activities of the poor tend to be highly diversified. The credit that is obtained is used as working capital to support the family unit in the various activities where the family units have become very efficient;
- (c) **The poor can save.** Evidence indicates that substantial savings can be generated by the poor, including, inter alia, through "forced" savings, such as deductions on loans, as in the case of the Grameen and Predom Banks. These small loans have proved to be very effective in reaching the poor.

78. In this context, it is important to reassess premises that may not have been questioned for some time, in the light of the emerging evidence. There is no doubt that in considering the large resource requirement for poverty reduction, the poor themselves are able to generate savings to invest in their betterment and provide other resources to uplift themselves and their communities. However, for this to happen, there is a need to address some of the factors contributing to general low domestic-resource mobilization, such as low (or negative) returns to financial savers as a result of low administered interest rates; lack of confidence in the banking system; and limited range of instruments of savings mobilization.

III. CONCLUDING REMARKS AND ISSUES FOR FURTHER DEBATE

79. The evidence reviewed in this section covers two decades of development and shows that given the massive and entrenched character of poverty, even a major shift in resources is not likely to be sufficient to address this issue in full measure. For a truly successful effort to reduce poverty, new resources must be generated at the local-community, national and international levels.¹⁸ There is an urgency in developing countries to mobilize domestic resources in the 1990s, in the face of declining inflow of foreign capital, which has resulted from a number of factors, including high indebtedness and slow growth in official development assistance.¹⁹ There is a pressing need for investment, particularly in the agricultural sector and other sectors directly related to the livelihood of the poor. There is a substantial gap between the investment required to attain the objectives of poverty reduction and alleviation and the domestic savings available in many developing countries.

80. The issue of determinants of household savings is crucial to domestic mobilization of resources. There is a need, at individual country level, to identify the significant determinants of savings and the policy implications. Some countries have demonstrated an ability to generate high rates of savings despite institutional and behavioural obstacles to savings mobilization. It would be instructive to examine how such deterrents have been overcome, in order to facilitate useful exchanges of experiences. In dealing with the poor, it might be useful to examine not only the level and rate of savings as policy targets, but the forms of savings as well which might in turn increase the size of total savings. There are many forms of non-financial savings (e.g. rice banks) that have served the poor well and which need to be encouraged and may be institutionalized.

81. It would appear that an effective strategy would be to promote and facilitate the mobilization of household savings and the efficient allocation of credit, with emphasis on improving the access of small farmers and entrepreneurs to financial services. Funds must be mobilized from the domestic non-corporate sector, which is a net saver. This entails the existence of growing and efficient financial intermediation.

82. There are four major building blocks in the development of such an efficient and sound financial system: restructuring of non-viable institutions; building of financial infrastructure; a supportive policy environment; and institutional development. There is evidence that the commercial approach might be more viable on a sustained basis than the often favoured approach that emphasizes subsidized credit, and more successful in promoting the development of the poor sectors of the economy in developing countries.

83. The Intergovernmental Group of Experts may wish to address the following questions:

- (a) What are the main impediments to enlarge access of the poor to credit? What measures should be adopted to remove these impediments in the various banking institutions operating in rural areas and informal sectors? (for example, improvement of credit/loan conditions and guarantee schemes according to the activities to be financed, specific targeting of vulnerable groups);
- (b) What kind of experiences have been gained in establishing complementarity between the various financing practices such as group versus individual approaches and the various traditional types of credit activities (conventional banks, community development funds, non-governmental organization (NGO) initiatives, etc.)?
- (c) How can access to credit schemes by potential entrepreneurs among the urban poor be increased so as to facilitate initial investments? How can

adverse selection by traditional financial institutions against such types of lending be eliminated? How could the activities of NGOs and community initiatives which can provide credit to groups involved in urban productive projects be facilitated?

84. It is important that policy planners and practitioners realize that increased resources nationally will not automatically translate into increased flows of resources to the poor. In fact, more often than not, fiscal policies may affect distribution of income in a manner that does not favour the poor. Purposeful government action is needed to ensure that the poor receive the resources necessary to improve their lot within the budgetary constraints that every country faces.

85. In this context, important issues which the Intergovernmental Group may wish to discuss would include:

- (a) What are the scope, ways and means for improving tax collection (and diminishing tax evasion), keeping in mind a poverty-alleviation perspective?
- (b) How could tax structures be reformed so as to enhance revenue mobilization, while ensuring that they are not regressive?

86. It is also important to ensure that reductions and stagnation in social expenditures do not disproportionately harm the poor. Equally important, the necessary policy reforms must be implemented to correct the inequities in the allocation of government social expenditures.

87. On the basis of their countries' experiences, members of the Intergovernmental Group of Experts may wish to examine the following:

- (a) The budget share which, across sectors, is devoted to rural development, especially in countries where poverty is mainly rural;
- (b) The priority given, within each social sector, to protecting or expanding basic services (primary education, basic health care, family planning, extension services, roads in remote areas, etc.);
- (c) The relative advantages of tax measures versus those of expenditure subsidies, as a means of income redistribution and poverty alleviation;
- (d) The scope for reduction of military spending in favour of social spending.

88. The intergovernmental Group of Experts may also wish, when discussing budgetary policies and exchanging experiences thereon, to examine the revenue and expenditure side of the budget together, as the availability of policy instruments which are efficient in alleviating poverty through income redistribution strongly influences the role of the revenue-raising side of the budget. However, if poverty alleviation can be carried out more efficiently through universal or targeted social expenditure programmes, then tax policy may focus on the efficiency aspect alone, without concern for the equity objective. In a consideration of different policy instruments, it would be thus important to discuss the trade-offs, if any, between efficiency and equity.

Notes

1. See for instance, Basil J. Moore et al: Domestic Savings in Selected Developing Asian Countries, Asian Development Bank Economic Staff Paper No. 2, Manila, Philippines.
2. The information in this paragraph and the next is adapted from Chapter III of The Least Developed Countries 1992 Report, United Nations, New York, 1993.
3. It is estimated that in Sri Lanka in 1980 more than 80 per cent of indirect taxes on tobacco, sugar and liquor fell on the poorest 40 per cent of households, while these taxes produced 28 per cent of total central government revenue. See, ILO "Income Policies in The Wider context : Wage, Price and Fiscal incentives in Developing countries". D. Pankert and D. Robinson (eds).
4. In most developing countries, it is not always certain that the poor derive as much benefit as the rich from public expenditure, but this is a problem to be tackled from the expenditure side of the government budget.
5. Livingstone and H. W. Ord : Economics for Eastern Africa, Ch 35. Heinemann, Nairobi.
6. Insofar as subsidies benefitted them. Many subsidies, however, do not benefit the poor directly (see below paras. 24-26).
7. The topic of the effects of structural adjustment programmes on poverty alleviation is on the provisional agenda of the second session of UNCTAD's Standing Committee on Poverty Alleviation.
8. David E. Sahn, "Public Expenditures in Sub-Saharan Africa during a Period of Economic Reforms", World Development Report Vol.20, No.5.
9. David E. Sahn, Ibid.
10. David E. Sahn, Ibid.
11. Because of low quality, however, an important point that can be made that primary education and health expenditures have mostly "benefitted" the poor, and hence been progressively distributed, as the non-poor avail themselves of private sector alternatives which are of better quality.
12. Source: US Arms Control and Disarmament Agency, World Military Expenditure and Arms Transfers, 1990, Washington, D.C. : United States Government Printing Office, November 1991, table 1 and United Nations Development Programme, Human Development Report 1991, New York Oxford University Press.
13. Idris Jazairy et al The State of World Rural Poverty: An Inquiry into its causes and consequences, IFAD, New York University Press.
14. See for instance : Wan-Soon Kim, Financial Development and Household Savings: Issues in Domestic Resource Mobilization in Asian Developing countries, Asian Development Bank Economic Staff Paper No. 10.
15. This could be in-kind or financial resources. There are many issues that need to be addressed. Some forms of credit lead to perpetual indebtedness of the poor.

16. See, for instance, United Nations Economic Commission for Africa, Agricultural Credit and the Mobilization of Resources in Rural Africa, 1986. E/ECA/PSD.4/9/Rev 1.
17. Mbat, David O., "Commercial Banks and Rural Banking Policy in a Developing Economy: Policy Implications", Savings and Development, No.4, VI, 1982.
18. Fontana, Francesco, "Credit and Agriculture in the Economy of Madagascar", Savings and Development, No.3, VII, 1983.
19. Aggrey-Mensah, W., "Small Borrower Guarantee Scheme - A Ghanaian Experience", paper for Workshop on Credit Guarantee Schemes held in Conakry, Guinea, 11-12 December 1980.
20. Economic Commission for Africa, Agricultural Credit and the Mobilization of resources in rural Africa, ECA, Addis Ababa, May 1986.
21. Burrows, J., and others, "The Second Decade: A Basic Economic Report on Kenya", Key Issues in the Private Sector (Report No. 201 KE, Vol.4, Annex), World Bank, 1974.
22. Adapted from M.K. Jogelkar and others, "Role of Credit Systems as Prime Mover for Rural Development", paper presented to the FAO-sponsored Seminar on Harnessing the Financial System in Support of Rural Development, India, July-August, 1981.
23. Bourne, Compton and Douglas H. Graham, "Problems with Specialized Agricultural Lenders:", in Undermining Rural Development with Cheap Credit, Dale, W., Adams et al, eds. (Boulder and London, Westview Press, 1984).
24. Abu-Shaikha, Ahmad, "Towards the Alleviation of Rural Poverty in the Sudan", WCARRD Follow-up Programme: In-depth Studies Series No.1, FAO, July 1983; quoted by ECA, Agricultural Credit and The Mobilization of resources in rural Africa, ECA, Addis Ababa, May 1986.
25. Schaefer-Kehnert, Walter, and J.D.von Pischke, "Agricultural Credit Policy in Developing Countries", World Bank Reprint Series, No.280, (1984).
26. Owusu, Kwame Opuku and William Tetteh, "An Experiment in Agricultural Credit: The Small Farmer Group Lending Programme in Ghana (1969-1980)", Savings and Development, No.1, VI (Milan, 1983).
27. Von Pischke, J.D., and John Rouse, "Selected Successful Experiences in Agricultural Credit and Rural Finance in Africa", Savings and Development, No.1, II, 1978.
28. Economic Commission for Africa, Report of the Regional Expert Consultation on the Role of Rural Cooperatives in the Productive Sectors in Africa, (ECA/SDEHSD/IRB/85/Rpt), October 1985.
29. Economic Commission for Africa, Ibid.
30. ILO, "Cooperatives in Food Production with Particular Reference to Food Storage and Security", ILO paper presented at the Regional Expert Consultation on the Role of Rural Cooperatives in the Productive Sectors in Africa, Addis Ababa, Ethiopia, October 1985.
31. Economic Commission for Africa, Ibid.

32. Anderson, R.T. (1966) "Rotating credit Associations in India", Economic Development and Cultural Change, Volume XIV.
33. This has been recognized by scholars as an outgrowth which is an adaptation to poverty: "Many of the traits of the subculture of poverty can be viewed as attempts at local solutions for problems not met by existing institutions and agencies because the people are not eligible for them. For example, unable to obtain credit from banks they are thrown upon their own resources and organize informal credit devices without interest", Lewis, Oscar (1961) Children of Sanchez, New York, Random House.
34. Timberg, T.A., and C. V. Aiyar (1984), "Informal Credit Markets in India", Economic Development and Cultural Change, Volume 33, No.1, October 1984.
35. Central Bank of Malaysia (1985), "Aspects of the Unorganized Money Market in Malaysia", Quarterly Economic Bulletin, Volume 18, No.4, December 1985.
36. The Poor are Bankable : Rural Credit, The IFAD way, IFAD, March 1987, Rome.
37. Henry R. Jackelen and Elisabeth Rhyne, "Towards a More Market-oriented Approach to Credit and Savings for the Poor", Mimeo (USAID and UNCDF).
38. See also World Summit for Social Development, including the role of the United Nations system in promoting Social Development, p.15 (document E/1993/77).
39. This is likely, in the present decade, to be exacerbated by the recession and increased unemployment currently affecting the developed countries.

ANNEX Table
Selected quasi-informal financial arrangements for the poor

Program	Country	Type	Year of Ref.	Years of Oper.	Total Beneficiaries	% who are women	Ave. loan size (\$)	% of loan funds in Arrears	Repayment rate (%)
ADEMI	Dominican Republic	NGO	1989	8	19,430 (88)	37	527	6.0	-
BKK	Indonesia	Quasi-govt.	1982	10	2,700,000	60	70	19.0	-
BRAC	Bangladesh	NGO	1987	18	169,000	55	31	-	92.5
BANCO DEL PACIFICO	Ecuador Bank	Prov.	1986	-	4,210	26	300	-	-
CAMCCUL	Cameroon	NGO	1988	20	68,000	25	2,264	24.0	-
GRAMEEN BANK	Bangladesh	Quasi-govt	1990	9	800,000	87	58	-	98.0
IDESI (Informal Sector)	Peru	-	1987	-	140,570	57.1	1,375	-	-
KUPEDES	Indonesia	Govt. bank	1989	5	1,380,000	25	425	5.4	95
PCRW	Nepal	Govt.	1989	8	6,640	100	59	-	90
FED	Ecuador	NGO	1989	4	2,937 (86)	71	1,150	0.05	-
PRODEM	Bolivia	NGO	1990	3	13,200	70	200	-	100
SAVING DEV. MOVEMENT	Zimbabwe	NGO	1984	10	250,000	97	-	0.03	-
SEWA	India	NGO	1982	14	40,000	100	72 (76-80)	-	90 (87)
SFDP	Nepal	Govt.	1989	15	78,520	14	74	-	48
WWF	India	NGO	1989	12	50,000	100	-	-	90-95

Source: Sh. L. Holt and H. Ribe "Developing Financial Institutions for the poor"; World Bank Discussion Paper No. 17, 1991, Washington, D.C.